AXIS DIRECT

12 MAR 2018 Company Update

# THOMAS COOK (INDIA)

MIDCAPS

**BUY**

Target Price: Rs 320

## Quess likely to be spun-off; stay invested

Thomas Cook's (TCIL) board has approved the proposal of a corporate restructuring exercise that would enable the company to focus on Travel-related businesses and give its shareholders direct exposure to Quess. **The contours as well as the timeline of the deal are yet to be disclosed.**

Our take: **(1)** In the scenario that existing shareholders are given Quess shares on pro-rata and no distribution tax is applicable, our estimates on residual business of Travel, forex and vacation ownership imply a 25% upside from CMP; **(2)** If distribution tax of ~20% is applied, **we recommend existing shareholders stay invested and not monetize Quess** – a steady compounder given immense opportunity landscape in business services tied directly to macro, shift from unorganized to organized, and consolidation of vendor base. Retain **BUY** on **TCIL** and **Quess**. Our estimates, TP remain unchanged.

| | |
|---|---|
| CMP | : Rs 256 |
| Potential Upside | : 25% |

**MARKET DATA**

| | |
|---|---|
| No. of Shares | : 367 mn |
| Free Float | : 32% |
| Market Cap | : Rs 94 bn |
| 52-week High/ Low | : Rs 274 / Rs 202 |
| Avg. Daily vol. (6mth) | : 413,216 shares |
| Bloomberg Code | : TC IB Equity |
| Promoters Holding | : 68% |
| FII / DII | : 6% / 14% |

**Exhibit 1: Our scenario analysis/calculations indicating upside from CMP**

| Particulars | Based on: | | Scenario 1 Distribution tax | Scenario 2 w/o Distribution Tax |
|---|---|---|---|---|
| Marketcap of Quess | Current Market Price | | 145,440 | 145,440 |
| Value of TCIL's 49% holding in Quess | | | 71,266 | 71,266 |
| **Post effective distribution tax of 20%** | | (i) | **57,012** | **71,266** |
| | | | | |
| Travel and Forex | 12x FY20E EBITDA | | 32,273 | 32,273 |
| Vacation Ownership | Sterling Holidays at 1.5.x Book value | | 13,050 | 13,050 |
| **Residual business valuation** | | (ii) | **45,323** | **45,323** |
| | | | | |
| **Effective valuation of TCIL based on our est** | | (i) + (ii) | **102,335** | **116,589** |
| Marketcap of TCIL | Current Market Price | | 93,310 | 93,310 |
| Upside | | | 10% | 25% |

Source:

**Financial summary (Consolidated)**

| Y/E March | FY17 | FY18E | FY19E | FY20E |
|---|---|---|---|---|
| Sales (Rs mn) | 85,880 | 112,139 | 136,876 | 157,119 |
| Adj PAT (Rs mn) | 382 | 2,027 | 4,048 | 5,595 |
| Con. EPS* (Rs.) | | 5.3 | 9.2 | 12.5 |
| EPS (Rs.) | 1.0 | 5.5 | 11.0 | 15.3 |
| Change YOY (%) | 112.2 | 431.0 | 99.7 | 38.2 |
| P/E (x) | 245.8 | 46.3 | 23.2 | 16.8 |
| RoE (%) | 2.8 | 12.5 | 21.0 | 23.2 |
| RoCE (%) | 11.6 | 14.9 | 19.3 | 20.8 |
| EV/EBITDA (x) | 29.8 | 19.3 | 12.9 | 10.0 |

Source: *Consensus broker estimates, Company, Axis Capital

**Price performance**

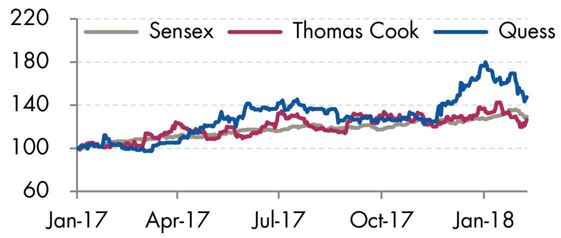

**Exhibit 2: SoTP-based TP of Rs 320 for TCIL**

| SoTP | EV (Rs mn) | Stake | Based on: |
|---|---|---|---|
| Travel and Forex | 32,273 | 100% | 12x FY20E EBITDA |
| Vacation Ownership | 13,050 | 100% | Sterling Holidays at 1.5x Book value |
| Human Resources | 69,025 | 49.0% | At 25x FY20E EBITDA, 20% holding co. discount |
| Debt | 12,935 | | As of FY17 |
| Cash | 13,760 | | As of FY17 |
| EV/share | 116,212 | | 364 mn shares outstanding |
| **TP** | 320 | | |
| **CMP** | 256 | | |
| **Upside** | 25% | | |

Source: Company, Axis Capital

We believe **Quess is a steady compounder** given the huge opportunity for business services in India

- Quess has created a formidable platform in the large business services space. Many businesses in India have been deciding that they can be more efficient, effective, and competitive if they buy certain services on the outside that they have hitherto taken care of internally.
- Given the size and scale of the opportunity, and the fragmented nature of the market, we believe that a large part of Quess' growth will be driven by inorganic roll ups. Quess has demonstrated successful acquisition track record with 4-5 year payback periods, margin accretive with ~20% RoE, and retention of key management personnel. Such deal flow and successful scale ups would not be available to a minority investor and needs to be backed by a company like Quess that has proven its ability to successfully turn around and integrate acquisitions.
- We believe Quess will continue to drive inorganic growth through tuck-in acquisitions, as part of its roll-up strategy, with the proceeds (~Rs 8.7 bn) of recently concluded IPP. While not currently baked in our numbers, this can potentially translate into EBITDA of ~Rs 10 bn over the next 3 years. We have a **BUY rating on Quess** with **TP of Rs 1,250** (30x FY20E EPS)

## Financial summary (Consolidated)

### Profit &loss (Rs mn)

| Y/E March | FY17 | FY18E | FY19E | FY20E |
|---|---|---|---|---|
| Net sales | 85,880 | 112,139 | 136,876 | 157,119 |
| Other operating income | - | - | - | - |
| Total operating income | 85,880 | 112,139 | 136,876 | 157,119 |
| Cost of goods sold | (33,712) | (40,370) | (49,275) | (56,563) |
| Gross profit | 52,168 | 71,769 | 87,600 | 100,557 |
| Gross margin (%) | 61 | 64 | 64 | 64 |
| Total operating expenses | (49,042) | (67,152) | (81,138) | (92,968) |
| EBITDA | 3,126 | 4,617 | 6,463 | 7,589 |
| EBITDA margin (%) | 4 | 4 | 5 | 5 |
| Depreciation | (846) | (1,105) | (1,349) | (1,548) |
| EBIT | 2,280 | 3,512 | 5,114 | 6,040 |
| Net interest | (1,309) | (1,812) | (1,742) | (1,672) |
| Other income | 944 | 1,376 | 1,722 | 2,270 |
| Profit before tax | 1,915 | 3,076 | 5,094 | 6,638 |
| Total taxation | (1,138) | (634) | (610) | (585) |
| Tax rate (%) | 59 | 21 | 12 | 9 |
| Profit after tax | 777 | 2,442 | 4,484 | 6,053 |
| Minorities | (395) | (415) | (435) | (457) |
| Profit/ Loss associate co(s) | - | - | - | - |
| Adjusted net profit | 382 | 2,027 | 4,048 | 5,595 |
| Adj. PAT margin (%) | 0 | 2 | 3 | 4 |
| Net non-recurring items | - | - | - | - |
| Reported net profit | 382 | 2,027 | 4,048 | 5,595 |

### Balance sheet (Rs mn)

| Y/E March | FY17 | FY18E | FY19E | FY20E |
|---|---|---|---|---|
| Paid-up capital | 367 | 367 | 367 | 367 |
| Reserves & surplus | 14,841 | 16,868 | 20,917 | 26,511 |
| Net worth | 18,015 | 20,183 | 24,379 | 30,128 |
| Borrowing | 12,935 | 12,435 | 11,935 | 11,435 |
| Other non-current liabilities | 1,021 | 1,021 | 1,021 | 1,021 |
| Total liabilities | 59,823 | 69,091 | 79,564 | 90,359 |
| Gross fixed assets | 26,762 | 26,467 | 26,416 | 26,564 |
| Less: Depreciation | (5,536) | (6,641) | (7,990) | (9,539) |
| Net fixed assets | 21,225 | 19,825 | 18,425 | 17,025 |
| Add: Capital WIP | 418 | 418 | 418 | 418 |
| Total fixed assets | 21,644 | 20,244 | 18,844 | 17,444 |
| Total Investment | 2,155 | 2,155 | 2,155 | 2,155 |
| Inventory | 75 | - | - | - |
| Debtors | 9,938 | 13,825 | 16,875 | 19,371 |
| Cash & bank | 13,760 | 17,217 | 22,694 | 29,399 |
| Loans & advances | 6,020 | 7,681 | 9,375 | 10,762 |
| Current liabilities | 27,853 | 35,453 | 42,230 | 47,776 |
| Net current assets | 29,794 | 38,723 | 48,944 | 59,531 |
| Other non-current assets | 6,230 | 7,969 | 9,621 | 11,229 |
| Total assets | 59,823 | 69,091 | 79,564 | 90,359 |

Source: Company, Axis Capital

### Cash flow (Rs mn)

| Y/E March | FY17 | FY18E | FY19E | FY20E |
|---|---|---|---|---|
| Profit before tax | 1,915 | 3,076 | 5,094 | 6,638 |
| Depreciation & Amortisation | (846) | (1,105) | (1,349) | (1,548) |
| Chg in working capital | 175 | 2,128 | 2,033 | 1,664 |
| CF from operations | 2,855 | 7,488 | 9,608 | 10,936 |
| Capital expenditure | (1,101) | (1,400) | (1,400) | (1,400) |
| CF from investing | (2,664) | (3,331) | (3,331) | (3,331) |
| Equity raised/ (repaid) | 67 | - | - | - |
| Debt raised/ (repaid) | 2,962 | (500) | (500) | (500) |
| Dividend paid | (166) | (200) | (300) | (400) |
| CF from financing | 1,551 | (700) | (800) | (900) |
| Net chg in cash | 1,742 | 3,457 | 5,477 | 6,705 |

### Key ratios

| Y/E March | FY17 | FY18E | FY19E | FY20E |
|---|---|---|---|---|
| OPERATIONAL | | | | |
| FDEPS (Rs) | 1.0 | 5.5 | 11.0 | 15.3 |
| CEPS (Rs) | 3.3 | 8.5 | 14.7 | 19.5 |
| DPS (Rs) | 0.0 | 0.0 | 0.0 | 0.0 |
| Dividend payout ratio (%) | 0.0 | 0.0 | 0.0 | 0.0 |
| GROWTH | | | | |
| Net sales (%) | 40.9 | 30.6 | 22.1 | 14.8 |
| EBITDA (%) | 69.5 | 47.7 | 40.0 | 17.4 |
| Adj net profit (%) | 138.9 | 431.0 | 99.7 | 38.2 |
| FDEPS (%) | 112.2 | 431.0 | 99.7 | 38.2 |
| PERFORMANCE | | | | |
| RoE (%) | 2.8 | 12.5 | 21.0 | 23.2 |
| RoCE (%) | 11.6 | 14.9 | 19.3 | 20.8 |
| EFFICIENCY | | | | |
| Asset turnover (x) | 5.7 | 6.9 | 9.4 | 12.2 |
| Sales/ total assets (x) | 1.6 | 1.7 | 1.8 | 1.8 |
| Working capital/ sales (x) | (0.1) | (0.1) | (0.1) | (0.1) |
| Receivable days | 42.2 | 45.0 | 45.0 | 45.0 |
| Inventory days | 0.3 | 0.0 | 0.0 | 0.0 |
| Payable days | 53.6 | 52.1 | 52.5 | 52.5 |
| FINANCIAL STABILITY | | | | |
| Total debt/ equity (x) | 0.8 | 0.7 | 0.5 | 0.4 |
| Net debt/ equity (x) | (0.1) | (0.3) | (0.5) | (0.7) |
| Current ratio (x) | 1.1 | 1.1 | 1.2 | 1.2 |
| Interest cover (x) | 1.7 | 1.9 | 2.9 | 3.6 |
| VALUATION | | | | |
| PE (x) | 245.8 | 46.3 | 23.2 | 16.8 |
| EV/ EBITDA (x) | 29.8 | 19.3 | 12.9 | 10.0 |
| EV/ Net sales (x) | 1.1 | 0.8 | 0.6 | 0.5 |
| PB (x) | 6.2 | 5.4 | 4.4 | 3.5 |
| Dividend yield (%) | 0.0 | 0.0 | 0.0 | 0.0 |
| Free cash flow yield (%) | 1.9 | 6.5 | 8.7 | 10.2 |

Source: Company, Axis Capital

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| SELL | Less than -10% |



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